A RAND NOTE

The Evolution of the European Economy: Implications for Transatlantic Relations

C. Cooper, J. Steinberg, M. Shires

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PREFACE

This Note examines the economic performance of the United States and Western Europe in the years since World War II and the likely impact of recent political and economic developments (especially the movement toward Western European integration) on future United States–Western European relations. It should be of interest to U.S. and European policymakers and analysts concerned with transatlantic trade and financial and political relations.

This Note was originally prepared for the second joint RAND-Instituto Affari Internazionali workshop on "The Southern Region and the Atlantic Alliance in a Changing Strategic Landscape," sponsored by The Ford Foundation. The workshop met at the IAI headquarters in Rome, Italy, on September 24–25, 1990, and included 32 participants from France, Germany, Italy, Portugal, Spain, the United States, and Turkey. It was updated and revised during the autumn of 1991 to take into account recent international developments and new data.

SUMMARY

Ever since the creation of the Atlantic Alliance and the launching of the Marshall Plan in the years following World War II, the United States has been the dominant voice in the transatlantic community. In recent years, however, both the security and economic dimensions of U.S. leadership have begun to erode. This erosion, coupled with a more integrated and stronger European economy, has led to a realignment of the transatlantic relationship.

European economic performance has converged with that of the United States in many areas. Furthermore, the increasing tendency of the European Community (EC) to act on behalf of its member countries has increased Europe's relative stature in the relationship.

Since World War II, the performance of the European economy has followed a somewhat different path than that of the United States. Until about 1970 growth rates of both Gross Domestic Product (GDP) and per capita GDP in Europe generally outpaced those in the United States. Subsequently, EC and U.S. GDP growth was roughly comparable, except during the first half of the 1980s when U.S. growth was more rapid. Over the entire postwar period, European per capita GDP has converged with that of the United States, fueled in part by an increase in European productivity in terms of output per employed person and output per man hour relative to that of the United States. Job creation, however, is one area where the United States economy has far outperformed its European counterparts, leading to convergence in the productivity growth rates between the two when measured in terms of output per working-age person. During this same period the European share of world trade has risen dramatically as a result of skyrocketing trade within the region.

The prospects for growth in the next decade for the United States are uncertain, although the more pessimistic forecasts seem unwarranted. The growth prospects for Europe depend on the outcome of several interrelated developments, including German unification, economic reform in central Europe and the Soviet Union, the EC-92 program and the associated prospects for a European economic and monetary union—as well as the demographics of the European marketplace. These events seem likely to bring about a relatively more prosperous Europe with several more countries at or near U.S. levels of per capita income. Economic disparities within Europe will decrease, and political and economic integration both within the EC and between EC and non-EC countries in Europe will increase substantially.

The emergence of a larger and more powerful European economy, combined with a reduction of U.S. dominance in the world economy, will lead to a more assertive European role in economic issues. Unilateral U.S. leadership in international economic and financial matters cannot be sustained, and the prospects of continued U.S. leadership in the liberalization of global trade are slim. Simultaneously, the economic integration of Europe and the move in Europe toward economic and monetary union (EMU) will strengthen Europe's negotiating position and will produce a uniquely European perspective. The result is that neither the United States nor Europe will be dominant in the economic relationship, and hence neither will be able to dictate policy preferences.

The political and economic changes in Europe will also force a change in the U.S.–European security relationship. The decline of the Soviet threat, combined with economic difficulties in the United States, makes it harder to sustain a costly U.S. overseas military presence. The emergence of an increasingly unified European voice on security issues also points to a stronger European role. The EC will increasingly replace individual European nations as the United States' interlocutor on important foreign policy and security issues in NATO (NATO has historically been the focus for U.S. leadership of the transatlantic community).

The integration of the European defense industry is another area that has particular significance for transatlantic relations. Recent trends in Europe have led to a significant breakdown of the heretofore strong national boundaries within the European Community, and the result has been a flurry of cross-border acquisitions, mergers, share exchanges, and strategic alliances among European high technology defense firms. U.S. firms and officials have expressed concern that there is a movement toward excluding U.S. industry from the European market. Many Europeans, however, point to U.S. restrictions on Europeans' access to the U.S. defense market. With the shrinking of western defense budgets, the potential for transatlantic friction in defense procurement is high.

While current trends point to an increased and stronger European role in the transatlantic relationship, the EC must still demonstrate its ability to play a leadership role in international economic and political affairs. It is not yet clear whether the EC will succeed in articulating a coherent European policy rather than simply balancing and coordinating its members' individual national interests.

Both the United States and Europe share a common interest in a thriving, open international economic system. Furthermore, both the United States and Europe recognize the need for a U.S. role in guaranteeing the security of Europe. As the balance in the transatlantic relationship shifts in the future, potential conflicts between Europe and the

United States over political and economic issues could cause more friction. Acceptance by the United States of a more balanced partnership with Europe, in return for Europe's willingness to overcome parochial preoccupations in economic affairs, would lay the basis for a new partnership in the transatlantic community.

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1. INTRODUCTION

Ever since the creation of the Atlantic Alliance and the launching of the Marshall Plan in the years following World War II, the United States has been the dominant voice in the transatlantic community. The military might of the United States, including its nuclear deterrent, formed the cornerstone of Western Europe's security throughout the Cold War. The economic strength of the United States made possible the postwar reconstruction of Europe, while the United States guided the building of international economic institutions that provided the framework for Western prosperity. This leadership entailed considerable costs—but offered corresponding benefits in the form of an ability to influence its allies' policies to support U.S. interests. In effect, the U.S.–European relationship took the form of a tacit bargain: in return for the U.S. commitment to maintain Western Europe's security and to encourage its economic growth, Europe would recognize the U.S. leadership in transatlantic affairs.

In recent years both the security and economic dimensions of U.S. leadership have begun to erode. With the end of the Cold War, the importance of the U.S. security guarantee to Europe has substantially diminished and U.S. economic strains have been reflected in persistent balance of payments and budget deficits. At the same time, an economically stronger and more self-confident Western Europe is forging a collective identity, and is becoming a more equal interlocutor for the United States.

In an earlier publication,[1] we analyzed the implications of the changing security environment for U.S.–European relations. In this Note, we examine the economic dimension of the transatlantic relationship and the consequences of growing economic parity.

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[1]"Political and Economic Issues Within the Alliance: The Future of Burdensharing and the Southern Region," James Steinberg and Charles Cooper, *The International Spectator*, April–June 1990, p. 128.

2. THE ECONOMIC RECORD

During the early postwar years, economic growth rates for most European countries exceeded those in the United States, due primarily to the process of European recovery and reconstruction. From 1950 to 1960, the European Community (EC)[1] countries grew at a 5.4% average annual rate, compared with 3.3% for the United States (see Table 1 in the Appendix). West German economic growth (8.9%) was particularly impressive during this period; British economic growth (2.8%) was notably lackluster. During the 1960s, the gap between the European growth rates (5.0%) and the U.S. growth rate (3.8%) continued, although they were converging. During the 1970s, U.S. (2.7%) and European (2.9%) growth rates were comparable, with France (3.3%) and Italy (3.1%) somewhat higher than the United States, Germany (2.7%) roughly the same, and the United Kingdom (1.9%) again lagging. From 1980 through 1985 the picture again changed, and although the United Kingdom's growth improved slightly to 2.0%, U.S. growth (2.7%) considerably outpaced that of the EC (1.5%) and the European Free Trade Association (EFTA) members (2.0%). This is the period that gave rise to apprehensions of long-term "Eurosclerosis"—endemic low rates of growth. During the period from 1985 to 1989, however, both the European and U.S. economies increased their average annual real Gross Domestic Product (GDP) growth rate substantially, to 3.1% and 3.4% respectively.

On a per capita basis, European growth, which took place during a period of little population growth, remained well ahead of the U.S. pace through the 1970s (2.4% to 1.6%) (see Appendix, Table 2). After a period of stagnation (1980–1985) when the United States outpaced the EC, the European performance improved again in the late 1980s, growing 20% faster than the United States (2.8% versus 2.3%). In 1960, average EC per capita income was only $1,051, while U.S. per capita income was $2,842 (see Appendix, Table 3). By 1980, the difference between the U.S. and European living standards had narrowed, with an average EC per capita income ($9,858) reaching 83.5% of the U.S. figure ($11,804). That ratio held steady in 1990 ($18,366 in Europe compared with $21,847 in the United States). Living standards within Western Europe converged for the most part.[2] Underlying Europe's

[1]In this Note, all references to the EC include the current 12 members of the Community, unless otherwise noted. Data from years when the Community's membership was smaller have been adjusted to assure comparability.

[2]Of the five poorest EC countries in 1960 (Portugal, Spain, Greece, Ireland and Italy), only Greece had a proportionately lower per capita income in 1990 compared with 1960 (37% of the EC average compared with 40% in 1960). Portugal's and Ireland's relative gains were modest, while Spain and Italy experienced significant increases compared with the EC average. Of the richer EC countries,

relatively favorable per capita economic performance was a continued increase in labor productivity. Output per employed worker and per man hour increased more rapidly than in the United States, due in part to a shift from agricultural to industrial employment and sustained high levels of capital investment in public infrastructure and manufacturing. As can be seen in Table 4 in the Appendix, U.S. labor productivity growth rates have consistently lagged behind those of its European counterparts over the past 40 years.

Traditional methods of measuring labor productivity do not, however, take into account the differences in workforce participation (see below). An alternative measure of labor productivity, GDP per working age person,[3] measures the productivity of the economy as a function of its underlying manpower availabilities. In this respect, the U.S. productivity growth still lagged behind the EC and EFTA (see Appendix, Table 5) until 1980, but a reversal occurred in the 1980s when U.S. productivity growth outstripped that of the EC substantially (1.6% to 0.5% for the period 1980 to 1985).

Job creation has been a weak element in Europe's postwar economic performance. After the oil shock of the early 1970s, the percentage of the working age population employed began to fall, and did not rebound until 1989. During this period, unemployment remained very high, and the labor force increased slowly. In the United States, by contrast, both employment and the labor force expanded substantially during the 1980s. New job creation in the United States was dramatic, though increases in labor productivity were not. Fueled by immigration and a particularly rapid increase in female new entrants into the labor force, the U.S. economy was a far more effective job machine in the 1980s. From 1963 to 1988, total U.S. employment increased from 70 million to 117 million, while the working age population increased from 113 million to 163 million, an increase in the percentage employed from 62% to 72% (Appendix, Table 6). For the EC over the same period, employment increased from 122 million to 130 million, while the working age population increased from 186 million to 219 million, a *decrease* in the percentage employed from 66% to 60%. For the period as a whole, the U.S. economy generated jobs for 94% of the increased working age population; the EC for only 26%. While the European economy achieved significant productivity gains, it generated few new jobs and attracted few new entrants into the labor force.

Denmark and Germany experienced relative gains, while Luxembourg, France, Belgium and the United Kingdom declined in relative terms. The results for the United Kingdom were most dramatic, slipping from 131% of the EC average in 1960 to 93% in 1990.

[3] "Working age" is defined as persons 15 to 64 years of age.

Foreign trade has played an important role in stimulating European growth in the last 40 years. Appendix Table 7 compares the growth of European, U.S., Japanese, and world trade from 1960 to 1990. The EC's share of world exports, including exports between EC countries, rose from 34% to 39%, while the U.S. share fell from 20% to 12%. Relative to GDP and population growth, European foreign trade is particularly impressive: in 1989, U.S. exports amounted to $1800 per person, and some 9% of GDP. Comparable figures for Germany were $4000 and 21%, for France $3400 and 20%, for the United Kingdom $3200 and 16%, and for Italy $2400 and 16%. The Netherlands leads the group with exports of $8300 per capita, amounting to some 55% of GDP.

Trade among the West European countries ("intra-trade") increased rapidly (Appendix, Table 8). Indeed, excluding intra-West European trade, Western Europe's share of total world exports has declined since 1950 (from 26% to 20%), although at a slower rate than the United States (25% to 17%). Intra-trade as a share of total West European foreign trade (EC plus EFTA) has increased from 49% in 1950 to 71% in 1990, and as a share of EC trade from 36% to 61%. Intra-West European trade has accounted for a progressively larger proportion of the foreign trade of individual Community members (see Appendix, Table 9). For example, intra-West European trade has increased from 25% of all foreign trade in 1950 for the United Kingdom to 63% in 1990, bringing the United Kingdom trade patterns much more closely in line with other EC countries. The growth in European intra-trade reflects, in part, the increased importance of intra-industry trade based on opportunities arising from economies of scale and specialization within sectors and industries in the region, in contrast to "old style" commerce based on trade between sectors and industries.

Relative to GDP, extra-Community foreign trade remained stable from 1960 to 1990 at around 9 percent; U.S. foreign trade, however, as a share of GDP rose significantly during that period from 4 percent to 11 percent for imports, and 5 percent to 9 percent for exports. Trade balances (Appendix, Table 10) are another important area of divergence between the European and U.S. economic experiences, especially during the 1980s. During this period both Europe and Japan showed marked increases in their trade surpluses (in Europe, from a deficit in 1980 of $81.3 billion to a surplus of $8.1 billion in 1990 and in Japan, from a deficit of $10.9 billion in 1980 to a surplus of $99.4 billion in 1990), although a significant portion of Europe's increased trade surpluses is related to the retreat of the second oil shock, which inflated its 1980 trade deficit (OPEC[4] accounted for $50.9 billion of the EC-12's 1980 deficit).

[4]The Organization of Petroleum Exporting Countries.

In contrast, the U.S. trade deficit increased substantially (from $10.9 billion in 1980 to $89.1 billion in 1990), with an attendant decline in U.S. net assets.

Although in the early and mid-eighties there was disagreement among economists over the degree to which a trade deficit is a sign of weakness (the U.S. over-consuming, saddling future generations with the bill) or a sign of strength (foreign investors flocking to higher real returns available in a dynamic U.S. market), there was a widespread consensus by the end of the decade that a significant improvement in U.S. competitiveness and trade performance had become essential. Improved U.S. export performance so far in 1991 may be a sign of a turnaround, even though this is due in part to a somewhat earlier and sharper recession in the United States than in other industrialized countries, and to a weak dollar.

3. EUROPEAN INTEGRATION

Europe's strong economic performance in recent years is closely associated with the process of economic integration. Although recently overshadowed by the revolutionary events of 1989–1991 in Eastern Europe and the Soviet Union, the decision of the European Council (EC heads of government) in June 1985 to complete the internal market by the end of 1992 ("EC-92") marked the beginning of a revolutionary transformation of the West European economy. The 1987 Single European Act (SEA) energized the European economy with the promise of a market of some 320 million people (now 340 million with the addition of the former German Democratic Republic), with few barriers to the free flow of goods, capital, services, or people.

The prospect of EC-92 dramatically revised expectations and contributed to improved European economic performance in the late 1980's (see Table 1). This in part reflects higher rates of domestic and foreign investment as firms position themselves for the new, post-1992 environment. The most significant departure from the mediocre economic performance of the early 1980s occurred in Germany, although the strains of economic unification are now threatening its performance. With growth of nearly 4% over the 1987–1990 period, a sizable trade surplus, a low rate of inflation, declining unemployment and a strong deutschemark, Germany provided the foundation for similar improvements in other EC countries. Inflation, in particular, has been reduced and differentials narrowed throughout the EC (see Appendix, Table 11). The United Kingdom is again the odd country out, with poor performance in output, growth, inflation, and balance of payments. It remains to be seen whether the United Kingdom's accession to the EC's Exchange Rate Mechanism (ERM) will contribute to a greater convergence of the United Kingdom's macroeconomic performance with other EC countries. Although unemployment rates in Western Europe continue to remain stubbornly high, on the whole the last three years have seen the EC economies converge on a pattern of 3%+ economic growth and moderate inflation. Foreign investors have responded; Japanese investors, for example, sold off some $9 billion of U.S. securities in the first half of 1990, and redirected investments towards Europe. In 1987, U.S. securities accounted for 51% of all Japanese purchases of foreign securities, while the EC accounted for 42%. In 1990, the U.S. accounted for only 16%, while the EC accounted for a hefty 61%.[1]

[1]Bruce Stokes, "Staking out Europe," *National Journal*, May 25, 1991, pp. 1224–1225.

As recently as 1985, it would have been appropriate to compare the U.S. economy with that of leading European economies taken individually. Today, because of the growing integration of Western Europe's national economies, it is also appropriate to make such comparisons with the EC as a whole. Economic output of the EC is roughly as large as that of the United States, per capita income differences have significantly narrowed, and the EC remains the largest trading partner to the rest of the world. European integration (as evidenced by the growth of intra-European trade) has steadily increased, and restrictions on internal European trade are diminishing.

There are also other signs of growing macroeconomic convergence and integration within the Community. Consumer prices, as measured by the average private consumption deflator, have dropped on average from 13.5% in 1980 to 5.1% in 1990.[2] Furthermore, growth in the nominal cost of labor has converged within the Community, decreasing from an average of 12.1% in 1980 to 6.2% in 1990. For participants in the ERM, this convergence has been even more dramatic, decreasing from an average of 7.6% in 1980 to 3.3% in 1990.[3] The dispersion of these growth rates betweeen these member states is also decreasing. These are further indicators of the growing economic integration between the member states of the European Community.

It is important, however, not to be too hasty in projecting an untroubled continuation of the current period of European economic prosperity. Just as the "Eurosclerosis" of the early 1980s gave way to "Europhoria," as some years earlier a supposedly permanent dollar shortage turned into a dollar glut, a reversal of Europe's economic fortunes could be in the offing, at least in the short term. The Iraqi invasion of Kuwait sent oil prices soaring, and impeded European growth through early 1991. The oil price increases occurred at a time when European firms' earnings were already below expectations, interest rates were tightening, and basic industries (autos, chemicals, and steel) were showing signs of weakness. The U.S. recession was mirrored by recession in much of Europe, where Germany was virtually alone in sustaining growth in 1991. German economic performance is expected to weaken considerably in 1992 in part as a result of the drain on resources needed to subsidize living standards in Eastern Germany. Nonetheless, the substantial real investments of recent years and expectations of efficiency benefits yet to come as EC-92 reforms take hold suggest that European economic performance will remain relatively strong over the decade ahead compared to the 1970s and early 1980s.

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[2]EC Commission, "Economic Convergence within the Community," *European Community*, No. 46, December 1990, pp. 152–153.

[3]*Ibid.*, p. 156.

4. WHAT LIES AHEAD IN THE 1990s

ECONOMIC GROWTH

The Europhoria that recently prevailed in the markets and in journalism left the impression that the European economy in the 1990s is likely to speed away from a lumbering U.S. economy mired in political and financial stalemate. This is by no means a sure bet. There is some prospect for improvement in the political, financial, and market conditions in the United States. Recent progress in reducing the U.S. external payments deficit may continue. Although the Persian Gulf War somewhat deferred and scaled back the anticipated "peace dividend," the decade as a whole is likely to see declining real U.S. defense spending and a falling defense share of national output. Coupled with progress in resolving the federal budget problem by bringing revenues more in line with non-capital federal outlays, this could provide a political foundation for long-run growth. Although U.S. financial institutions will remain fragile as a result of undercapitalization and imprudent lending policies in the 1980s (particularly if the U.S. recession persists), U.S. longer-term demographic trends remain more favorable than those in Europe. On the other hand, there are as yet only fragmentary signs that the current shakeout is leading to a reversal of the poor U.S. performance in productivity per employed worker, even though labor force growth will slow markedly. There also remains more talk than action in restoring U.S. technological leadership in critical sectors. On balance, recovery from the current recession when it occurs seems likely to bring solid, if not dramatically improved, U.S. economic performance over the next decade. There are as yet no indications of a prospective surge in U.S. productivity and growth.

For Europe, prospects for the future turn on assessing the effect of powerful new forces—German unification, economic reform in central Europe and the Soviet Union, EC-92, and a possible European economic and monetary union—and the interaction of those forces with enduring economic, political, and demographic variables that have traditionally influenced economic growth.

German Unification

Unified Germany has a population of some 80 million people, making it the largest European nation. However, the full economic consequences of German integration are not yet clear. It is already apparent that the costs and difficulties of integrating the two German economies were initially underestimated. In 1990 and 1991, unification has provided a

stimulus to the West German economy (an additional 1%–1.5% growth in 1990) with only a modest increase in inflation. Over time, the additional labor force available in the former East Germany could help to address a chronic West German labor shortage. The EC (and the U.S.) economies are likely to see increased exports to Germany as German trade and investment is directed inward, and consumption rises. But there remain many question marks, notably the consequences for overall German economic performance of continued large-scale transfers to East Germany to support wages and social payments.

The end of liquidity credits to East German firms is triggering what some have called an employment "massacre"—with unemployment rising rapidly and a sharp decline in East German GDP. How soon this decline can be turned around, and at what cost, remains uncertain. To achieve a reasonable degree of equivalence between personal incomes in East and West Germany, East German capital needs are estimated to be DM 500–1,000 billion over the next decade, at a time when most analysts expect other demands to significantly tighten world capital markets. Private investment has been slow to respond as basic questions such as property ownership are gradually sorted out. There will be significant strains on the German federal government budget, with the prospect of high deficits, rising real interest rates, and/or higher taxes. The overall effect on West German growth seems uncertain.

Eventually, German unification may produce more rapid German economic growth as efficiency and productivity improvements in Eastern Germany bring economic performance more in line with the education and skills of its labor force. The pace, timing, and distribution of additional growth is uncertain. Even if Eastern Germany achieves over 5% annual growth over the next decade, at the end of the decade it would still trail the western parts of Germany in per capita income by a significant margin. Moreover, German economic leadership in Europe has been based in part on the strength of its balance of payments, price stability, a firm deutschemark, and continuing success in containing inflation. The strains of unification have complicated Germany's ability to sustain its performance in each of these areas.

On balance, the economic outlook for Germany is for continued moderate to high rates of growth throughout the decade, in part as a result of a substantial substitution of domestic for overseas investment, but with per capita incomes in the East remaining well below those in Western Germany. It is conceivable, but less likely, that integrating the two Germanys will, after an initial adjustment period of several years, unleash a full-fledged economic boom in the East, dramatically reducing economic disparities throughout Germany. The other

extreme—protracted economic failure in Eastern Germany—seems less likely, but cannot yet be ruled out.

Economic Transition in Eastern Europe

The prospect for economic growth in Eastern Germany is in many ways more favorable than for Poland, Hungary, and the Czech and Slovak Federal Republic (CSFR). The reform process in the former GDR is even more "radical," the resources from both public and private sources available to support reform are far greater, and the institutional and legal framework provided by Western Germany obviate the need to start from scratch in building commercial, financial, legal, and accounting systems. However, Poland, Hungary, and the CSFR have one advantage: their ability to offer foreign investors the prospect of lower real wages for an extended period. By contrast, past German reform is complicated by the political need to reduce the standard of living differential between Eastern and Western Germany more rapidly than productivity gains would normally permit.

The industrialized countries may well provide significant external financial support, technology, and expertise to help bring about a successful outcome to economic reform in Eastern Europe, but the process of transforming these economies will take many years. The potential political and social strains in the near term are great, with a risk that popular opposition generated by economic hardship could thwart full implementation of needed reforms and thus seriously damage growth prospects. Opening markets for Central European exports in Western Europe may prove a greater stumbling block than external financial support, as global competition continues to compel rigorous adjustment and efficiency measures in the West European private sectors. Although the EC now seems prepared to adopt a more liberal trade regime with East European countries as part of the new EC–Eastern Europe "association" agreements, there are still powerful economic interests in Western Europe that will resist truly open access for East European goods and commodities. A critical question is whether Central European workers will find work at home or will be driven to seek jobs in the growing economies of Western Europe, with the possibility of serious political, economic, and social strains from large-scale population movements.

The Economic Consequences of EC-92 and European Monetary Integration

The Cecchini report,[1] published in 1988, concluded that implementing the Single European Act would provide a substantial one-time boost to European output (between 2.5%

[1]Paolo Cecchini (English edition, J. Robinson, ed.), *The European Challenge, 1992: The Benefits of a Single Market*, EC Commission, 1988.

and 6.5% above what would otherwise have been achieved), and subsequent studies have concluded that growth rate increases would be significant.[2] Economists have been busy ever since trying to sort out and quantify the implied scale effects and gains from specialization. While there are widely varying estimates of the effect on European growth of reduced internal barriers to trade, there is broad agreement that the gains will be substantial. Liberalized trading arrangements between the EC and the nations of EFTA and Central and Eastern Europe will intensify the impact of EC-92. The upsurge in European investment activity, including large-scale U.S. and Japanese investments to position overseas firms for the new opportunities and competition after 1992, lends considerable credence to such expectations. The burst of technological improvement accompanying the investment boom also augers well for the future.

The prospect of an early implementation of EC monetary integration [3] brings with it the possibility of even greater monetary and fiscal policy convergence and considerable economic benefits from reduced transaction costs.[4] "Possibility" does not mean "certainty," however. While a single currency would further reduce the costs of trade between countries with separate currencies, whether it will necessarily result in holding inflation in check is not so clear. Currency unions can be hard on some of the participants, as the present plight of Eastern Germany demonstrates. Indeed, it is precisely that dilemma that is raising questions whether the deutschemark can be counted on as the noninflationary anchor of an economic and monetary union (EMU). Implenting an EMU will require strong fiscal discipline in each of the members as well as an agreed-upon European strategy for regional aid, which could lead to further delays, and even a breakdown in the process.[5]

Demographic, Labor Force, and Social Policy Issues

A key question surrounding future European economic development is how a graying Europe, deeply committed to the social welfare state, will adjust to the prospect of little or no domestic labor force growth in a world of intense international competition. Germany's situation is somewhat unique, with the influx of workers from East Germany and Central

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[2]For example, see Richard Baldwin, "The Growth Effect of 1992," *Economic Policy*, October 1989, pp. 248–281.

[3]The European Council reached agreement at its December, 1991 summit on a timetable and procedures for adopting a single currency.

[4]The economic effects of monetary union were the subject of a recent EC study. The direct benefits of monetary union were estimated at an immediate increase of 0.4% in the Community's GDP. Indirect long-term effects of the monetary union in combination with economic union revised Cecchini's original estimate of a 2.5% to 6.5% boost to 3.6% to 13.6%. See the study, "One Market, One Money," *European Economy*, No. 44, October 1990.

[5]See below, pages 14–16.

Europe in 1989 and 1990. But even there the traditional domestic interplay of real wages, productivity and working conditions, and social policies will be the root of much domestic political debate and contention. A recent article in the *Financial Times* sums up the issue as follows: "The EC is starting from a weak base and facing difficult labor challenges with no real agreement about what to do. The creation of a single market has concentrated debate on two questions. One is how to prevent the new mobility of capital leveling down European wages by the 'social dumping' of plants in low-wage countries. The other is how to achieve the free movement of labour."[6] Internal net migration within the EC, for example, was only 25% of the U.S. rate from 1980–1985.[7] Labor mobility will be an increasingly important and controversial issue. Moreover, potential labor force entrants from Central and Eastern Europe, the former USSR, and the Mediterranean littoral are likely to pose significant social and political challenges. As discussed earlier, the EC nations' long-term record in creating new jobs and expanding the labor force is poor, although in 1988 this picture began to improve. It is not clear whether this improvement will be sustained; job creation could well remain the Achilles heel of European economic performance.

On balance, the removal of barriers to trade in Western Europe is likely to provide a foundation for higher annual growth rates during the 1990s in Western Europe, particularly for EC members, than those experienced in the early 1980s, with per capita growth rates above those in the United States. Because the United Kingdom's economy is relatively large and its performance relatively poor, improvements in its economic performance in the 1990s would make a particularly significant contribution overall to European economic prospects. A systemic failure of economic reform in Central Europe, on the other hand, would bring attendant crises of democratic governance and the likely eruption of national and ethnic violence and conflict that could damage the climate of stability that fostered the optimism of the late 1980s. Similarly, prolonged weakness in East German economic performance could have serious economic and political repercussions for Germany as a whole.

ECONOMIC AND POLITICAL INTEGRATION

The SEA's implementation has given a strong push to the process of both political and economic integration in Europe. The EC member states may fail to adopt implementing legislation for some of the approximately 280 directives that make up the single market program; tax harmonization is incomplete; and implementing the free movement of people

[6]*Financial Times*, September 5, 1990, p. 20.

[7]"One Market, One Money," *European Economy*, No. 44, October 1990.

remains controversial. Nevertheless, the psychological reality of the single market, coloring the economic and financial choices of Europe's public and private decisionmakers, is at hand.

The broad economic impact of the 1992 program will help reshape European industry. For example, the new regulations governing public procurement, which give contractors from all EC nations equal access to each others' transportation, telecommunication, water, and energy projects, represent a significant inroad in an area where national preference was most deeply ingrained, with substantial economic consequences. Procurement subject to the regulations is estimated at as much as 15% of GNP annually.[8]

The prospect that the EC will move further down the road toward EMU is the next important stage of this process. With the United Kingdom's and Portugal's accession, all members of the EC except Greece now participate in the Exchange Rate Mechanism, although the United Kingdom, Spain, and Portugal are allowed the more permissive 6% fluctuation in the value of their currency from the base rate (the others must remain within 2.25%). Despite considerable skepticism, nine of the twelve have ended all capital controls, and the remaining three have committed to doing so. The EMU's first phase is nearly complete, and all Community members now accept a significant constraint on their independence in macro-economic policies.

At the EC summit held in Maastricht on December 9–10, 1991, the European Council agreed on a plan for adopting EMU.[9] Prior to January 1, 1994, all EC states must abolish all capital controls and, if necessary, adopt a program to assure economic convergence with other EC members.[10] On January 1, 1994, the Economic Monetary Institute (EMI) will come into being, charged with strengthening the coordination of member states' monetary policies and preparing the procedures for implementing a single currency. By December 31, 1996 (at the latest), the European Council will review the extent of economic convergence, and if the Council finds (on the basis of a qualified majority vote) that a majority of the member states

[8]Nicholas Colchester and David Buchan, *EUROPOWER*, Economist Books, 1990, p. 93.

[9]The final treaty text on EMU was signed in February 1992. Substantial portions of the agreed-upon draft treaty are reprinted in *Financial Times*, December 12, 1991, and all quotations from the EMU agreement are found in that source.

[10]Under the agreement, convergence will be measured by four principal criteria: price stability (whether the inflation rate is close to the three best performing members of the Community); sustainability of the government's financial position (whether the annual budget deficit is 3% or less of GDP, and whether the total government debt is 60% or less of GDP); exchange rate stability in the European Monetary System (EMS) (whether the country has stayed within the permitted 2.25% band of fluctuation for at least two years); and durability of convergence (convergence of the government's long-term interest rates with other EC states). The Council will also consider other criteria, such as current account balance of payments and unit labor costs. Despite the high degree of specificity in some of the established criteria, the council retains flexibility in deciding whether a country on the whole has achieved the necessary degree of convergence to participate in the single currency.

meet the criteria,[11] it will set a date for beginning the single currency and creating a European System of Central Banks (ESCB) and a European Central Bank (ECB), which will manage the single currency.[12] Even if a majority of states do not meet the criteria by the end of 1997, a single currency will be adopted, beginning on January 1, 1999, for states that fulfill the conditions.

EMU will also mean increased Community control over member governments' fiscal policies. The Maastricht agreement prohibits European Central Bank financing of EC governments' debts, and authorizes the European Council to apply sanctions (including restrictions on borrowing from the European Investment Bank, requiring non–interest bearing deposits to be placed with the Community, or fines) in the event a nation runs persistently high budget deficits.

Although the framework and timing of EMU are now settled in principle, there remain many hurdles to its eventual implementation. If the EC criteria on convergence were applied to member countries' economic performance at the end of 1991, only France, Luxembourg and the United Kingdom would qualify (Germany's 3.6% of GDP budget deficit exceeds the 3% benchmark). Spain, Italy, and Portugal face significant challenges in meeting the criteria by 1997, while Greece (not yet even a member of the EMS) faces daunting obstacles. Nonetheless, the Maastricht agreement provides considerable new impetus to creating a single EC currency for most if not all members.

In parallel with progress toward EMU, the EC is pursuing closer political links, both by expanding the EC's sphere of jurisdiction and strengthening Community institutions. At Maastricht, the European Council agreed to establish a "European Union" which will include a "common foreign and security policy" eventually leading to the framing of a "common defence policy," closer coordination on police and immigration issues, new authority in the fields of health, environment and employment policy,[13] and enhanced powers for the European Parliament.

[11] To meet British political concerns, a protocol to the agreement provides that the United Kingdom is not obliged to participate in the final stage of creating a single currency without a separate decision by the British Parliament. The United Kingdom therefore does not count toward determining whether a majority of countries meet the criteria to enter into the single currency. Under the Danish Constitution, approval of the EMU agreement requires a referendum; if Denmark has not passed such a referendum by the appropriate time, it too will not count toward the necessary majority.

[12] The Council agreed that the ESCB and ECB will make "price stability" their primary objective. External exchange rate policy will also be conducted by the ECB, but the agreement provides that the European Council may conclude formal agreements with other countries on exchange rates, or "formulate general orientations for exchange rate policy."

[13] The United Kingdom refused to agree to the new "social" provisions governing employment and worker's rights; thus the new jurisdiction applies only to the other eleven countries, but will use the existing EC machinery.

Taken together, the agreements on economic and political union represent an important new phase in West European integration, which will shape EC members' relations not only with each other, but also with the United States and the international community.

BROADENING EUROPE

In the longer run, the process of European integration will extend well beyond the EC's twelve current members. Initially, integration will be led by economic relations, with the creation of a European Economic Area (EEA), encompassing the EC and EFTA,[14] and new association agreements with the countries of Eastern and Central Europe.[15]

Expanding EC economic relations with non-EC members will not only further integrate the European economy but will inevitably spill over into more institutionalized political relationships. For most of the EFTA countries—especially Austria and Sweden (which have already applied for EC membership)—the issue of future EC membership has moved to the forefront of national political debate.

The prospect of full EC membership is also a high priority for the Central and East European countries; in their view, it is the key to political stability as well as economic growth. While full membership will not come about quickly, bringing these nations into closer economic and political relations with the EC marks an important stage in creating wider European integration and would, in the interim, sustain their sense of European identity. The close link between economic and political relations can be seen in the EC's central role in coordinating economic assistance to the East European countries,[16] as well as the negotiations for EC association agreements, governing not only trade and investment but political relations as well. These efforts have deeply involved the EC in helping to shape the course of political as well as economic reform in Eastern Europe.

CONCLUSION

In summary, the marked reduction in internal barriers to commerce and investment in Europe over the next decade is likely to bring about

[14]The EC and EFTA leaders reached agreement on the EEA on October 22, 1991, but the accord must be ratified by all 19 countries' parliaments. This is not simply a formality, since there is considerable opposition in some of the affected EC states (notably Portugal), as well as in some EFTA countries.

[15]Poland, Czechoslovakia, and Hungary signed association agreements with the EC in December, 1991.

[16]Twenty-four industrialized nations of the OECD (G-24) that have agreed to assist East European democracies created the Phare program to channel economic and technical assistance, initially to Poland and Hungary, and later to Czechoslovakia, Bulgaria, and Romania. The June 1989 meeting of the G-7 (United States, Canada, Japan, France, Germany, Italy, and the United Kingdom) led to an agreement designating the EC to coordinate the aid.

- a relatively more prosperous Europe, with several countries at or near U.S. levels of per capita income;
- reduced intra-regional economic disparities;
- substantially increased political and economic integration within the EC; and
- closer relations, both economic and political, between the EC and non-EC countries in Europe, creating the prospect of a more unified European voice on a broad range of issues.

5. IMPLICATIONS OF GROWING ECONOMIC PARITY BETWEEN EUROPE AND THE UNITED STATES

Although Europe may grow faster than the United States in the 1990s, this by itself is unlikely to be the controlling factor in setting the terms of U.S.–European relations. A little faster growth on one or the other side of the Atlantic, marginal disparities in balance of trade and payments, or differences in inflation are peripheral to the more important changes that are taking shape in European governance. What will count far more is the extent to which Europe continues to develop a European regional identity, the degree of convergence of European national interests, and the progress toward creating institutions expressing and acting upon common interests. Europe's new sense of equality vis à vis the United States stems as much from the process of integration as from the raw statistics of size or economic performance. As long as European economic performance is adequate to sustain movement toward a more unified region, Europe will continue to be more assertive in its economic relations with the United States.

One consequence of effective economic parity is that the United States and Europe are increasingly dependent on each other's economic performance. Neither actor is dominant, so neither can dictate policy preferences. This is a marked change from the first decades of the postwar era, when enlightened U.S. leadership forged a liberal economic order, and its views held sway on international economic issues. Mutual economic dependence means more hard bargaining and a need to find mechanisms to replace unilateral U.S. decisions in order to maintain cooperation and discipline.

As economic competition intensifies, unilateral U.S. leadership in international economic and financial matters, already much weaker than it was through the 1970s, cannot be sustained. The United States appears to be increasingly unwilling to shoulder the political burden of this leadership, a burden that requires abjuring unilateral protectionist measures, even in the face of protectionism by U.S. trading partners. After the United States terminated the gold exchange standard in 1973, a series of subsequent U.S. trade actions, from the soybean embargo in 1974 to the provisions of the 1988 Trade Act, confirmed that the United States was no longer willing to remain above the fray.

The United States has been the driving force behind every round of postwar multilateral trade negotiations under General Agreement on Tariffs and Trade (GATT) auspices. The ambitious and critically important Uruguay Round, which began in 1986, is no exception, but is likely to mark the last time the United States provides the impetus for

global liberalization. Although the December 1990 breakdown in negotiations makes the previously unthinkable—an outright failure to reach agreement—all too possible, some sort of agreed outcome may yet emerge. But it remains open whether such an outcome will lay the basis for further multilateral liberalization or instead be seen as the last gasp of multilateralism.

What is at issue is whether an evolving multilateral international regime will remain the guiding force in the trade and investment issues arising in a rapidly globalizing market economy. On the table in the Uruguay Round, in addition to a general relaxation of trade restraints, are several important new areas currently not subject to multilateral discipline, including reducing agricultural subsidies and import restrictions, the future of the multi-fibres agreement governing trade in textiles, expanding open competition in public procurement beyond national governments, and extending GATT rules to intellectual property, services, and trade-related investment measures. Improvements in the GATT system itself are also on the agenda. The Uruguay Round carries considerable political significance: the tenor of future trade relations between the EC and the United States (agriculture is the key here) and between industrial countries and developing countries (which for the first time were prepared substantially to accept GATT rules with respect to their own trade).

Of all the critical issues under negotiation in the Uruguay Round, none is more important than liberalizing agricultural trade (which was exempted from GATT rules in 1955) and in particular, the reform of the EC's Common Agricultural Policy (CAP). The United States wants a commitment by all GATT parties to the principle of free trade in agriculture, expressed by converting quotas to tariffs, and then rapidly reducing the tariffs themselves (although congressional support for such a policy in sugar and dairy products is by no means assured). The EC will not accept such a commitment at this point, but is prepared to offer to reduce existing levels of protection now provided by the CAP. Events in Eastern Europe, and the spiraling costs of farm subsidies, may finally break the EC member states' resistance to CAP reform, paving the way for a GATT agreement in 1992. Freeing up agricultural trade is not only an issue between the United States and the EC; it is equally important to developing countries who see such liberalization as offering substantial export opportunities to their own agriculture. More than any other single issue, how far the EC is able to move to open up its protective agricultural policies will determine the long-term repercussions of the Uruguay Round.

While a successful conclusion to the Uruguay Round would help avoid a return to the beggar-thy-neighbor approach of the 1930s, there is now little prospect that the United

States can reassert unilateral leadership in world trade and investment matters. Without effective U.S. leadership in support of a liberal open international trade system, there is a real risk that the international economic system will cluster into three principal trade blocs—Europe, North America, and the Pacific—with relations among the blocs marked by negotiated access agreements rather than free and open trade. Such an outcome is likely to prove second-best for all countries, and a burden for many developing countries where sustained economic growth depends on further opening of the global economy. To avoid lapsing into bloc-to-bloc confrontations, there is a need for new collective leadership to replace the guiding hand of the United States, leadership which has failed to emerge in the 1980s.

Even if a successful outcome to the Uruguay Round is achieved, the international community must take further steps to maintain effective multilateral discipline over international trade and investment and forestall the continued proliferation of unilaterally determined exceptions, waivers, limitations, and preferences that have become such a prominent feature of trade and financial relations in the last few decades. Recent European expressions of concern about increased foreign competition after 1992, particularly from Japanese firms, have brought to the forefront hitherto dormant concerns. In this regard, the long overdue establishment of an International Trade Organization (ITO), originally intended as the international body to administer and enforce multilateral trade agreements, would be a possible next step for the international community. The lack of such an administrative body with legal enforcement powers has proved costly and is a major reason why GATT's dispute settling mechanisms are so inadequate and consequently increasingly eroded. The burgeoning of so-called "voluntary export restrictions" over the last fifteen years is one result. An ITO, or its functional equivalent, could take the lead in international trade matters and play the same kind of catalytic role in world trade and investment that the EC Commission has played with respect to intra-EC commerce. Regrettably, there now appears little likelihood this will occur.

In international finance, too, the absence of U.S. leadership has left a vacuum of authority. After some fifteen years of partly managed floating rates, there is still no consensus on what sort of systemic international exchange rate regime, if any, is needed. The present system has been tolerated in the absence of agreement on something better. Without consensus among major industrial countries on how the world's international money system should work, it has proved impossible to establish an effective oversight role for the IMF. G-7 meetings and agreements play a useful role in coordinating responses to current international financial issues as they arise, but a more comprehensive intellectual and

political foundation is needed to mobilize international institutions and policies in support of evolving global requirements.[1]

An EC decision to move forward on economic and monetary union could contribute significantly to filling the vacuum left by the diminished leadership of the United States and help to create an international financial system more capable of meeting the complex challenges of an increasingly global international economy. With monetary policy centralized at the EC level, the European Central Bank could well become the preeminent actor on interest rate policy, and the ecu the dominant reserve currency. The G-7 would de facto (if not de jure) become the G-4 on the most important aspects of international economic policy. Inevitably, U.S. influence over European economic policy would diminish, but a unified EC could provide the United States and Japan a more effective interlocutor on macroeconomic issues, thus paving the way to strengthened coordination and more stable international financial arrangements. Of course, the opposite could also happen: A more unified EC could become a more powerful economic adversary of the United States, complicating the search for international consensus and leading to less stable international economic and financial arrangements.

Growing economic parity between the United States and Europe will also have important consequences for the U.S.–European security relationship. As a result of growing European prosperity, enhanced European political integration, and diminished military threats, European nations will increasingly be able to provide for their own conventional defense. At the same time, these very factors will make it harder for the United States to sustain a costly overseas military presence in Europe. Although the U.S. nuclear guarantee is likely to remain an important component of Europe's geostrategic response to the residual military capability of the former Soviet republics (including their nuclear weapons), burdensharing considerations will inevitably lead to readjusting roles and responsibilities within the Alliance, with Europe playing a larger role.

More indirectly, the prospect that the heretofore European *Economic* Community will take on a security dimension means that the EC will increasingly become the United States' interlocutor on important foreign policy and security issues, instead of the individual

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[1]One issue that existing institutional arrangements are poorly suited to manage is the possibility of an emerging global capital shortage. An April 1991 report of the Bank for International Settlements documents the extraordinary surge of international capital flows in the 1980s but notes that among industrial countries in the latter half of the decade "capital imports have generally been used to sustain private consumption or public sector deficits or sometimes both. The aggregate ratio of saving and investment to income in the industrial world as a whole was much lower in the 1980s than it had been in previous decades, raising for many observers the spectre of a latent shortage of capital." Philip Turner, *Capital Flows In The 1980s; A Survey of Major Trends*, BIS Papers, Basle, Switzerland, No. 30, April 1991, p. 106.

European nations in NATO (a forum that has historically been the focus for U.S. leadership of the transatlantic community). This will lead to closer links between the economic and military dimensions of the U.S.–European relationship. This trend toward developing a West European security identity can already be seen in the role played by the Western European Union in coordinating the European naval response to the Iraqi invasion of Kuwait (August 1990), the growing influence of European Political Cooperation (EPC) in coordinating West European foreign policies, such as the response to the outbreak of fighting in Yugoslavia (June 1991), and the decision at Maastricht to establish a common foreign and security policy for the EC nations.

The movement toward a more European defense industry is an aspect of European defense integration that has particular significance for transatlantic relations, because it touches on important security as well as economic concerns. While detailed consideration of the nature and pace of the Europeanization of defense industries is beyond the scope of this Note, it is clear that the recent wave of cross-border acquisitions, mergers, share exchanges and strategic alliances among high technology European defense firms has begun to break down strong national barriers in Europe. Recent Independent European Program Group (IEPG) initiatives to open defense procurement to all member countries' firms point in the same direction.[2]

European defense and procurement officials have gone to great pains to dismiss suggestions that defense integration will come at the cost of excluding U.S. manufacturers from European procurement. But many Europeans point to U.S. restrictions on European access to the U.S. defense market, and argue that the only way to combat the U.S. firms' economic advantages is to grant Europeans preference in the European market. With shrinking Western defense budgets, declining export opportunities, and rising unit costs, the potential for transatlantic friction in defense procurement is considerable, as both the United States and Europe seek to protect their technological and industrial base.

But these are trends, not yet realities. Although European integration is moving forward, there are many hurdles to overcome. While Europe on paper is the equal of the United States in many ways, there is a vast difference between the effectiveness of a single government acting on behalf of its people, and the mixture of collective and individual national policies that is the Europe of today. The United Kingdom still resists the idea of a single currency or political union. Several south European EC nations are concerned that

[2]For an analysis of the evolution of European defense industrial integration and its impact on U.S.–European cooperation, see James B. Steinberg, *The Transformation of the European Defense Industry*, RAND, R-4141-ACQ, 1992.

economic and monetary union could hinder their ability to maintain competitiveness through adjusting fiscal and monetary policy. The long-run costs of German unification remain unclear. Competition and suspicion still infect the Franco-German relationship.

Most important, the EC has still to demonstrate that it can play a leadership role in international political and economic affairs, rather than simply balancing and coordinating its members' individual national interests. This is especially true in the realm of security affairs. While Europeans complained that they were asked to share the costs of the U.S. response to the Iraqi invasion without a say in the U.S. policy, the Europeans as a whole seemed content to let the United States take the initiative. Nor is it clear whether Europe can or will develop the political cohesion and military clout to act decisively against out-of-area threats, even if (judged on the ability to "afford" such capability) Europe is as well placed as the United States. And the United States is likely to remain the only country that can offer an adequate and politically acceptable nuclear guarantee to the non-nuclear states of Europe. This lack of European leadership is also apparent in the economic sphere—ranging from trade to international finance—where Europe still remains focused on promoting regional interests.

Taken together, these considerations suggest that growing economic parity by itself will not end the special leadership role of the United States in the Alliance. But economics in turn may undermine the U.S. ability to sustain its leadership role. If the United States chooses to devote indefinitely a significantly larger share of its GNP to defense than Europe and Japan, will it maintain long-term economic competitiveness with them? There are costs as well as benefits associated with being the world's only superpower, costs which the American taxpayer may become increasingly less willing to shoulder. The vituperative debate in the United States over the perceived inadequacy of the Allies' contribution to the Iraqi crisis could be a sign of things to come—captured in the *New York Times'* pointed headline, "A Superpower Goes Begging for Bucks."[3]

[3]*New York Times*, September 2, 1990, sec. 3, p. 1.

6. CONCLUSION

For the 40 years of the Cold War, Europe and the United States have been knit together in an alliance centered around a common military threat that required close collaboration and a commitment to subordinate national differences, especially in the economic realm, to the paramount common need to maintain transatlantic cohesion. With the end of the Cold War, the economic dimension of the U.S.–West Europe relationship will naturally come to the fore. The United States and Europe also share a common interest in a thriving, open international economic system, although parochial disputes have often obscured the broader areas of agreement and led to fears that economic conflicts could undermine transatlantic political cooperation in the future.

Economic integration is creating a more powerful European economy with the potential to rival the United States. But Europe has not yet developed the political and economic leadership consistent with its economic strength, leadership that is all the more important in light of constraints facing the United States in exercising a dominant economic and political role. A more united and assertive Europe could prove a more useful partner but also a more formidable competitor for the United States. The potential conflicts between Europe and the United States over political and economic issues could cause growing friction, unless leaders on both sides of the Atlantic take steps to create a new framework for U.S.–European relations. This argues that the United States accept a more balanced partnership with Europe, in return for Europe's willingness to overcome its parochial preoccupations in economic affairs and its reluctance to play a more active global role. Such a new partnership could form the cornerstone of a transatlantic community that would play a role similar to NATO's role in the Cold War era, reinforcing shared interests and concerns and providing a mechanism for resolving the disputes that are sure to arise.

Appendix

TABLES

Table 1

Average Annual Real Growth, Gross Domestic Product (In Percent)

Country	1950–1960	1960–1970	1970–1980	1980–1985	1985–1989
United States	3.3	3.8	2.7	2.7	3.4
EC-12*	5.4	5.0	2.9	1.5	3.1
France	5.1	6.1	3.3	1.5	3.0
West Germany	8.9	4.5	2.7	1.2	2.8
Italy	6.2	5.7	3.1	1.6	3.2
United Kingdom	2.8	2.9	1.9	2.0	3.6
EFTA	4.2	4.7	2.6	2.0	2.7

SOURCE: International Monetary Fund, *International Financial Statistics*, Washington, DC, various years.

*The European Community (EC-12) countries are Belgium, Denmark, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, and the United Kingdom.

**The European Free Trade Association consists of Austria, Finland, Iceland, Norway, Sweden, and Switzerland.

Table 2

Average Annual per Capita Real Growth (In Percent)

Country	1950–1960	1960–1970	1970–1980	1980–1985	1985–1989
United States	1.5	2.5	1.6	1.7	2.3
EC-12*	3.6	4.1	2.4	1.2	2.8
France	4.1	5.0	2.7	1.0	2.6
West Germany	7.8	3.5	2.6	1.3	2.5
Italy	5.6	4.9	2.6	1.4	3.1
United Kingdom	2.4	2.3	1.8	1.8	3.4
EFTA**	2.9	3.9	2.3	1.8	2.3

SOURCE: International Monetary Fund, *International Financial Statistics*, Washington, DC, various years.

*The European Community (EC-12) countries are Belgium, Denmark, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, and the United Kingdom.

**The European Free Trade Association consists of Austria, Finland, Iceland, Norway, Sweden, and Switzerland.

Table 3

Per Capita Gross Domestic Product
(Current Dollars)

Country	1960 Per Capita GDP	1960 Pct. of EC Average	1970 Per Capita GDP	1970 Pct. of EC Average	1980 Per Capita GDP	1980 Pct. of EC Average	1990 Per Capita GDP	1990 Pct. of EC Average	1960–1990 Factor of Change	*
Belgium	1,212	115%	2,616	114%	12,019	122%	19,321	105%	13.2	(–)
Denmark	1,291	123%	3,215	141%	12,991	132%	24,990	136%	16.1	(+)
France	1,334	127%	2.815	123%	12,365	125%	20,969	114%	13.0	(–)
Germany	1,299	124%	3,042	133%	13,250	134%	23,677	129%	15.1	(+)
Greece	419	40%	1,128	49%	4,159	42%	6,798	37%	13.5	(–)
Ireland	634	60%	1,317	58%	5,650	57%	11,873	65%	15.5	(+)
Italy	791	75%	2,002	88%	8,046	82%	18,884	103%	19.8	(+)
Luxembourg	1,682	160%	3,315	145%	12,609	128%	22,445	122%	11.1	(–)
Netherlands	1,021	97%	2,565	112%	12,006	122%	18,632	101%	15.1	(+)
Portugal	301	29%	740	32%	2,713	28%	6,031	33%	16.6	(+)
Spain	380	36%	1,110	49%	5,679	58%	12,413	68%	27.1	(+)
United Kingdom	1,381	131%	2,225	97%	9,529	97%	17,183	94%	10.3	(–)
EC Average	1,051	100%	2,286	100%	9,858	100%	18,366	100%	14.5	
United States	2,842		4,922		11,804		21,847		6.4	
Japan	472		1.946		9,088		23,316		40.9	

SOURCE: Statistical Annex, *European Economy*, No. 46, December 1990, pp. 221, 226; Eurostat.

*(+) indicates change was greater than EC average.

(–) indicates change was less than EC average.

Table 4

Growth Rates of Labor Productivity (Percentage Growth in GDP per Man Hour)

Country	1950–1960	1960–1970	1970–1980	1980–1988*
Canada	3.09	2.72	1.83	1.50
France	4.39	5.38	4.09	2.40
Germany	6.64	5.29	4.50	1.90
Italy	4.27	6.69	3.91	1.60
Japan	5.57	9.96	5.03	3.10
United Kingdom	2.19	3.56	2.77	2.60
United States	2.41	2.51	1.92	0.90

SOURCE: W. Baumol, S. Blackman and E. Wolff, *Productivity and American Leadership*, MIT Press, Cambridge, MA, 1989, p. 88; United Nations, *World Economic Survey*, New York, 1990, p. 172.

*For 1980-1988, figures represent percentage growth in output per person employed.

Table 5

Growth in GDP per Working-Age Person (In Percent)

Country	1950–1960	1960–1970	1970–1980	1980–1985
United States	2.3	2.1	0.9	1.6
EC-12*	3.7	4.4	2.2	0.5
EFTA**	3.2	3.9	2.2	1.3

SOURCE: Organisation for Economic Co-operation and Development, *Labour Force Statistics*, Paris, various years; International Monetary Fund, *International Financial Statistics*, New York, various years.

*The European Community (EC-12) countries are Belgium, Denmark, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, and the United Kingdom.

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Table 6

Employment Growth in the United States and Europe, 1963–1988
Total Employment
(In Millions of People)

Country	1963	1970	1980	1986	1988	Changes 1963-1988
United States						
Ages 15-64	113.0	127.0	150.8	160.4	162.9	49.9
Total employment	69.8	86.8	100.9	111.3	116.7	46.9
Unemployment	4.1	4.1	7.6	8.2	6.7	
EC						
Ages 15–64	185.9	191.9	205.8	216.9	219.0	33.1
Total employment	121.8	123.5	126.5	124.8	130.3	8.5
Unemployment	2.5	3.1	8.4	15.7	14.8	
OECD–Europe						
Ages 15-64	220.9	230.6	251.5	268.5	272.5	51.6
Total employment	147.9	150.4	156.5	156.8	163.5	15.3
Unemployment	4.0	5.1	10.5	18.0	17.0	

Percentage of Working-Age Population Employed

	1963	1970	1980	1986	1988
United States	62%	64%	67%	69%	72%
EC	66%	64%	61%	58%	60%
OECD–Europe	67%	67%	62%	58%	60%

Growth in Employment as Percent of Increase in Working-Age Population

United States	94%
EC	26%
OECD-Europe	30%

SOURCE: Organisation for Economic Co-operation and Development, *Labour Force Statistics*, various years.

Table 7

Changes in World Trade Patterns, 1950–1990
Exports: (F.O.B.) Billions of Dollars

Country	1950	1960	1970	1980	1990
United States	10.28	20.59	43.22	220.79	404.03
EC-12*	17.21	43.21	116.74	691.31	1360.95
EFTA**	3.12	7.51	19.62	111.64	236.65
Japan	0.82	4.06	19.32	130.44	311.22
World	50.57	131.49	282.10	1868.80	3446.50
Exports as Percentage of World Exports					
United States	20%	16%	15%	12%	12%
EC-12*	34%	33%	41%	37%	39%
EFTA**	6%	6%	7%	6%	7%
Japan	2%	3%	7%	7%	9%
Total	62%	57%	71%	62%	67%

SOURCE: United Nations Conference on Trade and Development, *Handbook of International Trade and Development Statistics*, New York, 1988.

*The European Community (EC-12) countries are Belgium, Denmark, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, and the United Kingdom.

**The European Free Trade Association consists of Austria, Finland, Iceland, Norway, Sweden, and Switzerland.

Table 8

European Intra-Trade Exports as Percentage of Total Exports

Country	1950	1960	1970	1980	1990
EC-12*	36%	41%	53%	56%	61%
EC-12* + EFTA**	49%	56%	66%	67%	71%

SOURCE: International Monetary Fund, *Directory of Trade Statistics*, Washington, DC, various years.

*The European Community (EC-12) countries are Belgium, Denmark, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, and the United Kingdom.

**The European Free Trade Association consists of Austria, Finland, Iceland, Norway, Sweden, and Switzerland.

Table 9

European Intra-Trade as Percentage of Total Trade (Exports and Imports)

Country	1950	1960	1970	1980	1990
Belgium/Luxembourg	56	66	76	75	80
Denmark	81	76	74	75	77
France	36	44	63	58	67
Germany	57	57	65	64	67
Greece	49	52	60	48	69
Ireland	75	74	74	78	76
Italy	42	50	57	56	67
Netherlands	62	67	74	71	77
Portugal	47	54	59	59	79
Spain	28	54	50	43	68
United Kingdom	25	32	43	56	63
Total EC*	47	54	65	66	71

SOURCE: International Monetary Fund, *Directory of Trade Statistics*, Washington, DC, various years.

* European Community.

Table 10

Trade Balance (In Billions of Dollars)

Country	1950	1960	1970	1980	1990
EC-12*	–3.8	–3.6	–8.1	–81.3	8.1
United States	1.4	5.5	0.8	–6.2	–89.1
Japan	–0.2	-0.4	0.4	–0.9	99.4

SOURCE: International Monetary Fund, *Directory of Trade Statistics*, Washington, DC, various years.

*The European Community (EC-12) countries are Belgium, Denmark, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, and the United Kingdom.

Table 11

Inflation Rates

Country	Average 1980–1983	Average 1987–1990*
Belgium	7.7%	2.3%
Denmark	10.3%	4.0%
France	12.0%	3.2%
Germany	5.1%	1.8%
Greece	22.6%	16.0%
Ireland	16.6%	3.2%
Italy	18.0%	5.6%
Luxembourg	8.1%	2.1%
Netherlands	5.5%	0.9%
Portugal	21.1%	11.2%
Spain	14.2%	5.9%
United Kingdom	10.8%	6.6%

SOURCE: International Monetary Fund, *International Financial Statistics*, Washington, DC, various years.

*Based on the consumer price index.